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SUMMARY

DEFICIT SHRINKS BY $127 BILLION

THE ADMINISTRATION'S MID-SESSION BUDGET REVIEW FOR FISCAL YEARS 2007-11

11 July 2006

Another surge in revenue – resulting from continued economic growth – has reduced the current-year budget deficit by $127 billion, compared with the administration's February projection, according to the revised estimates for the President's budget released today by the Office of Management and Budget [OMB]. This *Mid-Session Review* – an annual update of the budget – contains revised estimates of the deficit, receipts, outlays, and budget authority for fiscal years 2006-11, based on the latest available budget and economic figures.

The administration's figures include costs for Hurricane Katrina recovery efforts and estimated supplemental costs for operations in Iraq and Afghanistan in fiscal year 2007, as well as a bridge fund for fiscal year 2008.

The revised budget estimates are summarized in the table below:

Mid-Session Review Budget Estimates
(by fiscal year; dollars in billions)

	2005	2006	2007	2008	2009	2010	2011
Receipts	2,154	2,400	2,459	2,659	2,772	2,930	3,098
Outlays	2,472	2,696	2,798	2,847	2,929	3,053	3,224
Deficit	-318	-296	-339	-188	-157	-123	-127
Deficit as % of GDP	-2.6	-2.3	-2.4	-1.3	-1.0	-0.8	-0.7
Memorandum							
February Deficit Estimate	-318	-423	-354	-223	-208	-183	-205

Source: Office of Management and Budget

Key facts from the update include the following:

- **The Deficit is Falling Rapidly.** The administration estimates that the fiscal year 2006 deficit will shrink to $296 billion, which is $127 billion below its budget estimate in February. The administration also projects that the fiscal year 2004 deficit of $412 billion will be reduced by more than half in 2008, a year earlier than originally targeted.
  As a share of the Nation's economy, the deficit is projected to fall to 2.3 percent of gross domestic product [GDP] this year, and to 1.3 percent in 2008.

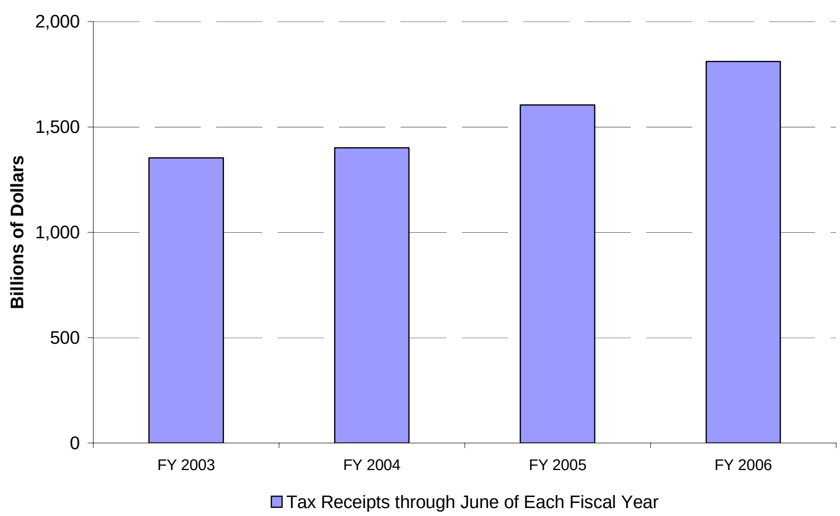
  - Compared with its February estimates, the administration has increased its spending projections to include supplemental costs for operations in Iraq and Afghanistan. These increases total $60 billion in 2007 and $50 billion in 2008.

- The administration's figures do show a deficit increase to $339 billion in fiscal year 2007. This is mostly due to an increase (compared with OMB's February estimates) in anticipated supplemental funding in 2007, and from changes Congress made in the 2006 supplemental and the tax extenders package as proposed by the President in February.

- The administration also projects that debt held by the public will decline as a share of the economy from 37.3 percent of GDP this year to 34.5 percent in 2011.

□ **Revenue Continues to Surge.** Strong growth in revenue – a product of the ongoing economic expansion – accounts for 90 percent of the deficit decline since the administration's February budget submission. Revenue has increased by 13 percent from this time a year ago, and is expected to grow by 11 percent for the full year. This will make 2006 the third consecutive annual increase in receipts, and the second straight year of double-digit revenue growth. *This revenue growth is occurring even under the continuing policy of sharply lowered tax burdens.*

Tax Receipts on Upswing Since 2003



- Receipts collected by the Federal Government were revised upward by $115 billion in fiscal year 2006, according to the *Mid-Session Review*. Receipts increased due to continuing stronger-than-expected economic growth – averaging 4.0 percent since 2003, compared to the post-World War II average of 3.4 percent per year.

- This strong growth, in tandem with newly created jobs and less than 5-percent unemployment for much of the year, has in turn translated into $60 billion in additional tax receipts for individuals.

- Individual income tax receipts have increased by more than 14 percent per year for the past 2 years, according to the Congressional Budget Office [CBO].

Although non-withheld taxes (including quarterly tax filings and taxes paid on capital gains) drove the growth in receipts last year, in 2006 regular withholding and payroll taxes have grown more, reflecting rising salaries and wages for individuals.

- The estimate for corporate tax receipts was revised upward by $53 billion because of record-high corporate profits as low interest rates, calm inflation, and labor productivity growth of 3.3 percent per year since the beginning of 2001 have increased the overall competitiveness of companies. Corporate tax receipts have grown by more than 25 percent per year for the past 3 years – largely because of corporate profits, according to the Congressional Budget Office.

- Finally, fiscal year 2006 receipts were revised up to reflect congressional variations to the administration's tax relief proposals included in the February estimate.

The administration also projects continued, sustainable growth over the next several years:

- Following the first quarter's 5.6-percent growth in inflation-adjusted GDP, the administration projects 3.5-percent growth for all of 2006. The administration projects growth in real (inflation-adjusted) gross domestic product [GDP] at or above 3 percent for the next 5 years.

- The administration also notes that the economy has created 5.4 million jobs since August 2003, and that the current unemployment rate – 4.6 percent – is lower than the average rates of the 1960s, 1970s, 1980s, or 1990s. The administration estimates unemployment will remain below 5 percent for the next 5 years.

- The estimates are consistent with those of the consensus of Blue Chip forecasters, and *assume extending current tax law, including the tax relief provisions of 2001 and 2003*.

- **Spending Restraint Under Way.** As reflected by the administration's figures, Congress has taken initial steps in restraining overall government spending, even while absorbing costs for Iraq and Afghanistan, and for Hurricane Katrina recovery. These efforts have included the Deficit Reduction Act of 2005, which will save $40 billion in mandatory spending over 5 years, and an across-the-board reduction in non-security discretionary appropriations for fiscal year 2006.

- **The Budget Control Effort is Not Complete.** Nevertheless, the current success at deficit reduction will not be enough by itself to meet the budgetary challenges approaching near the end of this decade.

  - In particular, the administration notes the continued projected growth of entitlements – particularly Medicare, Medicaid, and Social Security – noting that spending in the programs "will grow to the point that it will crowd out the rest of the Federal budget if needed reforms are not made." Overall mandatory spending now consumes about 53 percent of the budget, according to administration figures, and will grow to more than 60 percent over the next 10 years if programs are not reformed.

- In addition, the administration renewed its call for a line-item veto, and urged the Senate to pass such a reform. The House last month passed The Legislative Line Item Veto Act of 2006 (H.R. 4890), which would require Congress to vote up or down on enacted spending or tax provisions that the President calls into question.

(The estimates in the *Mid-Session Review* are based on the assumption that the President's policies are adopted. The Congressional Budget Office is scheduled to release its mid-year update of the budget – based on current policies – in mid-August.)